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ORIGINAL

MEMORANDUM

TO: Docket Control Center

FROM: Steven M. Olea
Director
Utilities Division

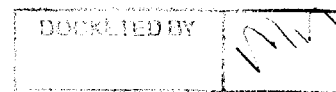
DATE: January 25, 2010

RE: WILHOIT WATER COMPANY, INC. – BLUE HILLS NO. 3 SYSTEM - REQUEST
FOR EXTENSION OF TIME OF COMPLIANCE ITEM (DOCKET NOS.
W-02065A-07-0313 AND W-02065A-08-0139)

Arizona Corporation Commission

DOCKETED

JAN 25 2010



In Decision No. 70658, dated December 22, 2008, the Arizona Corporation Commission ("Commission") approved the application of Wilhoit Water Company, Inc. – Blue Hills No. 3 System ("Wilhoit - Blue Hills No. 3 System" or "Company") for a permanent rate increase and approval of financing.

As part of Decision No. 70658, the Commission ordered that Wilhoit – Blue Hills No. 3 System provide:

"...by December 31, 2009, with the Commissions Docket Control, as a compliance item in this docket, a copy of the ADEQ Certificate of Approval of Construction for the arsenic treatment system."

On May 21, 2007, Wilhoit – Blue Hills No. 3 System filed an application for a permanent rate increase with the Commission. On November 9, 2007, Staff docketed its Staff Report recommending which included the implementation of an arsenic removal surcharge mechanism ("ARSM") for the costs of addressing arsenic in the Wilhoit – Blue Hills No. 3 System's water and, additionally, recommended approval of long term debt for the Company related to the ARSM. However, no financing case vehicle existed at that time as the Company had not previously filed a financing application in conjunction with the pending rate application. Therefore, on January 3, 2008, per Staff's recommendation and via Procedural Order, the Company was ordered to file an application for financing approval in conjunction with the pending rate case. The Procedural Order also required suspension of the rate case time-frame until Staff could analyze the financing application and file an amended Staff Report covering both the rate and financing applications.

On March 6, 2008, in Docket No. W-02065A-08-0139, the Company filed a financing application for \$40,000 in long-term debt to fund the costs of the arsenic treatment system. On May 7, 2008, Staff docketed an amended Staff Report for the rate case application (Docket No. W-02065A-07-0313) and financing application in which it recommended the same \$40,000 in

long-term debt authority. In Decision No 70658, dated December 22, 2008, the Commission ultimately ordered that the Company be authorized to issue up to \$70,000 in long-term debt for construction of an arsenic treatment system. Finally, via a Procedural Order, dated June 12, 2008, the stated dockets were consolidated by the Commission.

On December 11, 2009, Wilhoit – Blue Hills No. 3 System docketed a filing with the Commission, requesting an extension of time from the current December 31, 2009 due date until August 1, 2010 for the provision of the required AOC. The Company stated that they only recently received notification that their application for loan with the Water Infrastructure Finance Authority (“WIFA”) was approved. However, the loan must still be closed and these loan funds are patently necessary for construction of the additional storage. Finally, the Company states that “because of the delay in obtaining financing and the uncertainty of the ADEQ review process, the Company respectfully requests an extension of time to file the AOC until August 1, 2010.”

On January 11, 2010, Staff contacted Ms. Angie Valenzuela, Senior Loan Officer of WIFA, to discuss the Wilhoit – Blue Hills No. 3 System request for extension of time. Ms. Valenzuela stated that the Company’s loan application went to the WIFA Board of Directors and was approved on October 14, 2009. Since the loan was approved, the loan documents were sent to the Company on November 13, 2009. However, she noted that the loan closing has not taken place. Typically, the loan documents are reviewed by the Company and must be agreed to before closing can take place. In a previous conversation with Ms. Judy Navarrete, Executive Director of WIFA, it was stated that the Environmental Protection Agency now has new labor law requirements, relating to the Davis-Bacon Act, which the Company must allot for and include in the Company’s construction contracts. Ms. Navarrete implied that this would add additional time to the processing of the loan paperwork and the closing of the loan.

On January 8, 2010, Staff contacted Mr. Jim West, Company consultant, to discuss the Company’s request for extension of time and the processing of the loan closing. Mr. West stated that the approval was received from WIFA but the remainder of the entire process has been compromised by the effects of the Davis-Bacon Act. Mr. West went on to clarify that, in addition to increasing the loan processing and closing time, he expects the requirements of the Davis-Bacon Act to increase the actual costs associated with the storage project by approximately 15-20 percent. These costs were not considered when the Company received loan approval from the Commission in Decision No. 70953 and he stated that the Commission authority is no longer technically sufficient for the project. Mr. West has commented that he has been waiting on information from Staff to determine the appropriate action to take in order to address the pending shortfall in the Commission authorization.

When viewing the application and considering the previous decisions, Staff became concerned about the Company’s ability to see this loan finalized and the construction completed. Decision No. 70658 was issued on December 22, 2008 and ordered compliance with the required AOC by December 31, 2009. Staff must remind the Company that it has already utilized the entire period granted by this Commission and that it is currently out of

compliance with the AOC requirement for the arsenic treatment system. In that time, the Company has only been able to receive authorization of the loan from WIFA.

Further, the Company application requested an extension of time until August 1, 2010 for the provision of the required AOC. In order to meet that new date, the Company would still need to complete closing on the loan, apply for and receive the ATC, contract with a construction firm, see construction completed and apply for and receive the AOC – all within a little more than six months. The Company faces a difficult task that may not be easily accomplished.

One notable fact that Mr. West communicated was that the financing originally approved for the Wilhoit – Blue Hills No. 3 System was approved utilizing a surcharge mechanism that was to be calculated when the loan was finalized. While it is the Company's responsibility to consider and decide on the appropriate action, if the original authority/funding was organized via a surcharge mechanism, a solution is available. Staff believes that the Company should file, if needed, an additional loan application for the possible incremental increase in authority required. If the additional loan amount is approved by the Commission, then the required surcharge calculation would be made to address the new, higher authorization amount. The Company is responsible for considering its options, but some option should be selected and implemented quickly.

In summary, the swift processing of the WIFA loan is a vital and necessary element in the Company completing the construction and providing the AOC to the Commission. Staff therefore does not object to the Company proposal for extension of time for provision of the AOC related to the arsenic treatment system. However, Staff recommends that the Commission extend the due date of the AOC until December 31, 2010, to provide the Company with some sufficient time to complete the project. Staff further recommends that no further extensions be granted in this matter.

SMO:BKB:lhbm

Originator: Brian K. Bozzo

SERVICE LIST FOR:
DOCKET NOS.

WILHOIT WATER COMPANY, INC.
W-02065A-07-0313 and W-02065A-08-0139

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